Winter Could Test Energy Math; Rising Heat Costs May Be Last Straw For Family Budgets

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The next blow from high energy prices could come in the dead of winter. Utilities and industry analysts estimate that it will cost families 30% to 50% more to heat their homes with natural gas this winter. Families who use heating oil could face increases of between 50% and 100%. That is altering the math for consumers and energy companies alike. Some worry the higher heating costs could be the tipping point for family budgets that are struggling to absorb higher food and gasoline prices. Mark Wolfe, executive director of the National Energy Assistance Directors' Association, which represents state officials who administer energy relief funds, says many New England families could run a tab of $1,600 to $1,700 a month to cover heating oil, electricity and gasoline costs next winter. "I don't see any way to make the numbers work for middle-income people," he says, adding, "They're already shopping at Wal-Mart and eating out less. They'll have to cut back everything that makes them middle class. At some point, you're poor."

Governors, state attorneys general and other officials are calling on Congress to boost federal funding of the primary national energy assistance program, called Low Income Home Energy Assistance Program, or Liheap. At the current funding level of $2.57 billion, it helps only 17% of the nation's poor. The average annual grant for 2008 is $359. But as heating prices rise, those funds will not buy as much.

Utilities and heating-oil suppliers are also worried about their own exposure as more of their customers fall behind on their bills. Last winter, the average price of natural gas on the New York Mercantile Exchange was $7.71 a million British thermal units for the November-to-March heating period, according to the American Gas Association. The price for the coming heating season is expected to be about $13 a unit, up 67%. Roughly half of all U.S. households, about 54 million, heat with natural gas.

In a July 10 report, the U.S. Energy Information Administration said wholesale natural gas prices will average $11.86 per million cubic feet in 2008, up 65% from the average price of $7.17 in 2007. It expects the price to dip slightly to $11.62 next year. Consumers pay an even higher price because they must pay for gas storage, transportation and their local utility's costs, add-ons that will push the delivered cost above $15 a unit for homes, according to the EIA.

Kevin Rooney, the head of the Oil Heat Institute of Long Island, an association of heating oil suppliers, says that people could wind up paying $5 a gallon for heating oil this winter, a 72% increase from last year. About eight million households use heating oil, most of them in the Northeast and mid-Atlantic region. "In the past we worried about the elderly and the working poor," he says. "There are programs out there for them. This year it's going to be a middle-class phenomenon."

In New York state, there was a 41% increase in shutoffs of utility services among people who did not pay their bills in April 2008 versus April 2007, to 31,305 from 22,209, according to the Public Service Commission. (Utilities are prohibited from shutting off customers for part of each winter but restrictions lift in April.)

Many of the heating-oil retailers are small firms that are ill-equipped to handle the increased up-front costs. While they need to pay their suppliers within a few weeks, their customers often need 30 days or more to settle their bills. Some are worried they might be caught short.

Ray Hart, president and founder of Hart Petroleum on Long Island, says his customers are already asking for 100-gallon deliveries instead of filling their tanks, which can be 250 gallons or larger. An average-sized home on Long Island consumes about 900 gallons of oil a year for heat and hot water, creating a $4,500 expense. "If we have a cold winter, where's the money going to come from?" he asks. "You're looking at a terrible situation."

In Boston, Massachusetts Attorney General Martha Coakley is working to identify warming centers -- where families without adequate home heating can take refuge on cold nights. "I'm telling police and fire departments to prepare for 911 calls when people run out of heat," she says.

High costs may prompt more conservation and efficiency spending, much the way high gasoline prices are causing people to stick closer to home this summer. The past three winters, residential use of natural gas dropped about 5% each season nationally, amid volatile pricing. Many observers expect the drop in consumption to accelerate as people make changes to permanently reduce use.

Businesses and institutions are trying to figure out how they can lower their bills this winter. The University of Massachusetts at Amherst is replacing a 1940s coal-burning power plant with one that can burn either natural gas or heating oil, allowing the school to choose whichever fuel is more affordable.

In Farmville, Va., Longwood University is installing meters on most of its 75 buildings to identify which warrant efficiency upgrades. Dallas Theological Seminary is being paid $20,000 a year in exchange for allowing electricity to be cut off in grid emergencies. "We wouldn't even have considered it in the past when costs were lower," says Kevin Folsom, director of facilities.

Natural-gas utilities are offering free gas furnaces and other enticements to switch to natural gas from heating oil. Leonard Zangas, whose company, Vision Enterprises, owns and manages about 4,500 housing units in New York, is converting several buildings in

Manhattan and Queens to natural gas to save on fuel costs, he says, and because "Consolidated Edison [the local utility] is paying for half our conversion costs."

Heating oil retailers are fighting back, stressing that the run up in oil costs has been so dramatic that it can't stick. They're also advocating modest upgrades --like adding programmable thermostats, at $150 to $300 apiece, and better burners, at $800 to $1,000 - to cut heating oil use by 15% to 18%.

High prices are exposing some institutional weaknesses, too. In many states, utility regulators discourage utilities from buying natural gas under multiyear contracts. So when spot prices rise sharply, there's no buffer because high costs aren't diluted by purchases made at lower prices over longer periods of time.

In New York, utility regulators prefer Consolidated Edison make natural gas purchases no more than one year ahead of consumption whereas they allow electricity purchases as long as three years. Regulators say they'd prefer to have competitive gas suppliers perform the hedging function rather than regulated utilities. As a practical matter, though, that leaves many of Consolidated Edison's one million gas customers exposed because few gas resellers want to serve residential users.

The situation is worse than in 2005 when hurricanes ripped through the Gulf Coast, knocking out oil and gas production, because there are no easy fixes this time. Natural gas prices are coupled to oil prices and thus consumers are being taken on the same nauseating roller-coaster ride. Families haven't had time to adjust.

High prices have stimulated drilling activity but natural gas storage levels still are 2% below the five-year average. One reason is that U.S. imports of liquefied natural gas have sagged as U.S. buyers are outbid by buyers in Asia and Europe. Some re-gas terminals serving North America are operating at 10% to 15% of capacity, according to the American Gas Association. The negative outlook is causing utilities to take another look at how they cover their fixed costs. Two thirds of the industry uses old-fashioned rate structures that reward utilities for selling more units of natural gas each year. Given an upswing in delinquent accounts, growing numbers of utilities are getting permission to impose monthly charges, often $25 or more, to cover fixed expenses even if overall revenues fall because consumers cut back on energy use.